Learning to manage and control interfirm relationships

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English summary

In this dissertation, we have explored a complementary line of enquiry. First, we have examined how learning can inform subsequent control design such that firms learn to manage the exchange hazards more effectively. The ability to design more effective control systems for interfirm relationships is often considered as an opportunity to create competitive advantage. Hence, this should ultimately result in higher performance of cooperative relationships. The second part of this dissertation therefore focused on how combinations between different learning processes have an effect on the performance of cooperative relationships.

Although scholars have begun to examine the evolution of interfirm relationships empirically (e.g. Doz, 1996; Arino and de la Torre, 1998; Ring and van de Ven, 1994; Reuer and Arino, 2002; Arino et al., 2008; Faems et al., 2008), understanding of the processes underlying control changes in interfirm relationships is still limited. In addition, prior studies that have focused on the relation between learning processes and control adjustment have mainly examined this relationship within relationships (Arino and De la Torre, 1998; Dekker, 2004; Kamminga and Van der Meer-Kooistra, 2007; Langfield-Smith, 2008; Lumineau et al., 2011; Li et al., 2013), or across relationships with the same partner (Anand and Khanna, 2000; Faems et al., 2008; Dekker and Van den Abbeele, 2010). The contribution of the study reported in chapter 2 is that it not only examines control changes within relationships, but also how these control choices made in a prior relationship inform subsequent control choices in a relationship with a different partner. We find that the firms in our case studies experienced several difficulties in the management and control of their first partnering relationship. Although the extent of potential control problems in their second relationship were similar, the firms intentionally decided to use a less complete control structure in their second relationships rather than attempting to increase the detail and reliance on formal control. Experience in cooperating with another firm can therefore provide a better idea of what to anticipate in a cooperative relationships and help to form a better picture of what is required in order to successfully complete it, but this does not necessarily implicate that firms use this knowledge to reduce the incompleteness in the control design of subsequent relationships. Our results indicate that it created an urgency to facilitate learning about the transaction features and how these could be effectively governed. We also find that their reasons for this decision differ based on the performance of their prior relationship.

Prior research indicates that learning from success involves a different learning process than learning from failure, which also influences subsequent behavior and choices (Doz, 1996; Madsen and Desai, 2010; Diwas et al., 2013). After a success, people tend to conclude that they already have the appropriate knowledge needed to manage a situation and are not very active in acquiring additional information for improvement (Diwas et al., 2013). Failure indicates that the current way of operating is inadequate and therefore creates an urgency to search for alternatives that likely lead to the adoption of new and divergent procedures (March, 1981). As such, it creates a willingness to engage in different improvement activities, for instance by using different sources for acquiring new information and processing information by using a different perspective (Diwas et al., 2013). Our results show that the failure experience at the first case company indeed resulted in a different approach for their second relationships. They decided to use a less detailed contract and complemented control with the establishment of a relationship management team that became responsible for the day-to-day management of the relationships. By that, it served as a tight control mechanism in the daily operations of the relationships. As such, the failure resulted in an increased need for the outsourcing firm to safeguard their interests and objectives, and also have more flexibility and involvement in the coordination of the relationship activities. In their first relationship they tried to include more detail in the contract in order to align interests and expectations, but this relationship still resulted in a failure. The company therefore became reluctant to specify a detailed contract as they had serious doubts about the effectiveness of contracts to govern the outsourcing task and they changed the focus of control in their second relationships to behavior and processes instead of outcomes. On the other hand, we find that the second case company's management perceived their first relationship as successful which resulted in an intend to economize on subsequent renegotiation costs for the second relationship. As such, the successful relationships increased their trust in the value of detailed contracts. Using an incomplete contract was a design choice in order to first resolve the task uncertainties and facilitate learning about the intentions and expectations of the partner. By using this agreed on period to learn the task characteristics and each other's objectives and expectations, they were able to design a more effective and efficient contract that was completely understood by both partners. This not only increased the commitment of both partners to the task and each other, but was also expected to reduce future renegotiations costs. The performance of

prior relationships can therefore significantly influence the willingness of firms to engage in contingency planning activities in the beginning of new relationships.

In the first study, we have also focused on how specific learning processes – experiential, vicarious and deliberate - influence decision-making of individuals involved in managing cooperative relationships. Prior research has mainly focused on the effectiveness of specific learning processes and this has led to calls for more refined views of relationships between different types of learning processes (Schreiner et al., 2009; Lumineau et al., 2011; Arino et al., 2014; Heimeriks et al., 2015; Wang and Rajagopalan, 2015). The results of our case studies indeed indicate that firms use learning mechanisms differently over time, based on their experience. The effectiveness of learning mechanisms might therefore be dependent on how capable individuals are in using these mechanisms, which is probably informed by their level of experience. Based on the results of our case studies, we identified interactions with either the same or with different partners and the availability of deliberate learning mechanism (such as a relationship management team) as specific processes that had a significant influence on the decision making in the outsourcing relationships. We therefore focused on interactions between these processes in the other two studies of this dissertation, and specifically examined how these could influence the performance of cooperative arrangements.

In the second study conducted in this dissertation we examined how different types and sequential combinations of partnering experiences influence the performance of both current and subsequent cooperative relationships. With this study, we extend prior research on the contribution of both explorative and exploitative learning processes. While prior studies have shown that the simultaneous combination of these processes can result in resource allocation trade-offs and conflicting routines, we examine sequential combinations and uncover boundary conditions that affect positive and negative experience spillovers from prior interactions. We contribute to the literature by providing understanding about specific sequences of partnering strategies that could facilitate the development of cooperative management capabilities and what the relevant contingencies are in this process. We find that during initial experience, participants that interact repetitively with the same partner perform better than participants that interact repetitively with different partners. Our results also underline that these interactions with the same partner can be characterized as trustworthy and that partners need less time and attention for assessing each other's cooperative commitment, which induces fast and efficient decision-

making with the partner. This provides support for our argument that interactions with the same partner create a shadow of the future, and a stable and over time predictable interaction environment that contributes to the efficiency of learning. Although variety of experiences from interactions with different partners is considered to be beneficial in the long-term as it creates a capability to manage changes (Sampson, 2005; Zollo, 2009), we find that it constrains cooperative performance in the short term when individuals lack prior experiences. An explanation for these findings is that the highly perceived risk of opportunistic behavior by the partner lowers the ability to learn how to successfully cooperate with partners and does not stimulate partners to communicate integratively.

When transaction conditions change and make cooperative success relatively easy to achieve, participants that have learned how to cooperate with a specific partner during their initial experience are able to exploit this capability with an unfamiliar partner and there is no performance difference between participants subsequently interacting with a single partner and participants interacting with different partners. As such, if prior experience has permitted to develop trust in cooperation and common understanding about how the cooperate, it subsequently reduces behavioral uncertainty during interactions with different partners and low transaction risks. Additionally, their use of integrative communication, which is comparable to the proportion of integrative communication used by participants that continue to interact with a single partner, explains how they transfer their prior learning. This finding proposes a dynamic approach of learning to manage cooperative relationships, which initially requires relatively homogeneous experience such that learning is facilitated by avoiding too much causal ambiguity. Prior research indicates that participants with initial general partnering experience could be slow to subsequently learn how to cooperate with the same partner, as they could have developed some skepticism about cooperative intentions of partners. Our results however indicate that they are able to quickly adapt to this new interaction environment, as their performance does not differ from the performance of participants with initial partner specific experience. The relatively low resource investment that is required for cooperative success and the shadow of the future with a single partner seem to mitigate any negative perceptions about cooperative intentions of partners created during prior experiences. Only participants that continue to interact with different partners have difficulty to adapt to cooperative norms. This is also confirmed by our mediation analysis, which shows that their lower profits are partly explained by their lower use

of integrative communication. This points to the crucial role of interaction conditions in the learning process. When individuals do not have the opportunity to learn how to cooperate with partners, this discourages cooperative incentives.

When interfirm success becomes more difficult to achieve after a period of easy conditions, we find that participants interacting with a single partner perform better than participants interacting with different partners, and this effect is independent of the participant's initial experience. While an initially learned cooperative routine can be successfully exploited with different partners when there is relatively low environmental uncertainty, this cooperative routine is gradually replaced by a more competitive attitude under transaction conditions that make interfirm success difficult to achieve. Once these participants have experienced interfirm success with relatively low resource investments, they are not willing to increase their resource commitments to the cooperation. As this results in cooperation failures they subsequently start to protect themselves against opportunistic behavior of partners. We further find that participants with only partner specific experience perform significantly better than participants that started with partner specific experience and subsequently had general partnering experience and also better than participants that only had general partnering experience. But if participants have initial general partnering experience and subsequent partner specific experience, they do not perform significantly better than both treatment groups of subsequently different partners. This does indicate that when transaction conditions make interfirm success difficult to achieve, continuity in terms of stable relationships over time positively influences interfirm performance. In our mediation analysis we find that perceived cooperativeness of the partner during the initial experience has a significant direct effect on profit in subsequent interactions. This provides support for our argument that when prior partnering interactions created skepticism about partner intentions this can reduce the willingness to increase cooperative commitment when transaction conditions make interfirm success relatively difficult to achieve. While prior studies have argued that more variety in prior experiences results in a capability to be more responsive to contextual changes, we show that prior experiences also affect how individuals respond to different forms of contextual changes. Although our results can be dependent on the specific sequence of changes (first a change to less difficult and then a change to more difficult) that we implemented, it does show that variety in initial experiences can create enduring skepticism about cooperative intentions of partners, which can result in falsely attributing subsequent failure to partners.

In the third study conducted in this dissertation we focused on the interaction effects between experiential learning and deliberate learning. Specifically, we examined how different combinations in partnering experience and an ability to store knowledge of prior partnering interactions for future decisions influence performance of cooperative relationships. We hypothesized that stored partnering knowledge could increase the speed of learning how to successfully cooperate when individuals are inexperienced and interact repetitively with the same partner, as they could use this knowledge to verify the actions and decisions of the partners and identify potential improvements. Our results however indicate that during initial experience, interactions with the same partner result in higher profits, but access to more knowledge from prior experiences does not accelerate this process. We also expected that the potential benefits of having more variety of knowledge available to identify opportunities for improvement, as a result of interactions with different partners, would be completely offset be the cognitive limitations of interactions with different partners. Although we do not find a significant interaction effect on profit, we do find that participants interacting with different partners use more integrative communication and take more time to make their decisions when they have access to stored knowledge. As such, the knowledge is perceived as useful, but they have difficulties in identifying causal relationships and subsequently using the knowledge in the coordination of the task with a new partner. This suggests that participants are initially focused on resolving the behavioral uncertainty and need time to develop a capability to appropriately incorporate knowledge from prior interactions in their decision-making in order to speed up the value creation process.

We expected no additional positive effect of knowledge storage when participants with partner specific experience subsequently started to interact with a new partner in repetitive transaction with less difficult conditions. The ability to transfer prior established routines quickly results in trust in the new partner and lowers the need for additional information. Our analysis confirms this expectation. When transaction conditions make cooperative success relatively easy to achieve, knowledge storage does significantly improve the profit of participants interacting with different partners. In addition, we find that profits of participants with different partners and access to stored knowledge are not statistically different from profits of participants interacting with the same partner (either with or without access to stored knowledge). Our mediation analyses shows that their larger knowledge base helps them to communicate more cooperatively

and that this consequently results in higher profits. As such, it serves as a mean to both recognize the value of cooperative success and as an instrument to convince partners of cooperative intentions. Together these results suggest that participants interacting with different partners first need time to learn how to do the task before they can benefit from a larger knowledge base and that low environmental uncertainty can facilitate this process.

Finally, we show that stored partnering knowledge negatively affects profits when participants have partner specific experiences and engage in a new relationship that makes cooperative success more difficult to achieve. Having access to knowledge of prior successful actions increases the likelihood that decision-makers will stick with these routines. In dynamic environments, where conditions can differ substantially, this increases the risk of inappropriate generalization. With this study we therefore contribute to the literature by providing evidence that deliberate learning mechanisms can encourage overconfidence in partnering capabilities and experience-based rigidity. While prior studies have shown that competency traps occur at the dyadic level (Hoang and Rothaermel, 2005), we show that it also transfers across relationships. When managers become less aware and responsive to contextual changes in relationships, they could expose their firms to higher risks of cooperative failures.

The results of our case study can have practical value for firms that are relatively inexperienced in managing cooperative relationships, especially in outsourcing and buyer-supplier contexts that are often governed by contracts. In these situations, the buyer is usually not an expert in the product or service that it intends to buy, which is often the main reason for buying (Vanneste and Puranam, 2010). However, this inability to create a detailed and fully specified contract before the actual start of the relationships is not necessarily a disadvantage. Our results indicate that the outsourcing firms were able to complement incomplete contracts with behavioral controls directed at frequent information sharing and interactions between partners. This created the expertise necessary to set up more efficient governance structures and can therefore even provide a means to economize on subsequent renegotiations costs. This stresses the importance of following a learning strategy in which practical experience is used to improve control.

The results of our first experimental study provide more insight regarding specific strategic sequences that can facilitate the development of a capability to manage cooperative relationships which different contextual constraints. It specifically proposes that firms start off

with relatively homogeneous experiences and should avoid too much causal ambiguity in the beginning of their partnering experiences, as cognitive limitations of individuals hamper their ability to learn from these experiences. In addition, this causal ambiguity can increase the risk of cooperative failure, which can create skepticism about cooperative intentions of partners, which can result in incorrect attributions of failure in subsequent relationships. Finally, our result of the second experimental study can have practical relevance for firms that use specific departments, functions or management teams for their interfirm relationships. We acknowledge that understanding about what caused success in different cooperative contexts experienced requires an explicit investment in retrospective sense-making, which can be encouraged and facilitated by deliberate learning mechanisms (Zollo and Winter, 2002). However, firms should be careful in establishing best practices or standardized protocols of interfirm management as this could potentially result in inertial forces or even overconfidence and overestimating the firms' partnering capabilities. This dissertation therefore has potential broader implications related to the importance of installing particular processes and structures that determine and prescribe a firm's partnering management practices. While these processes and structures can enhance efficiency in stable environments, the desire for reliability and accountability can exacerbate the tendency to do what has been done before (Mayer and Bercovitz, 2008). However there can be occasions when forgetting is functional. Overemphasizing and -reliance on routinized processes and structures can encourage rigidity and superstitious learning. Enhancing learning requires that individuals are also encouraged to update and refine their partnering practices such that they are more timely and context appropriate. Forgetting or unlearning what has been learned in the past is therefore sometimes an organizational necessity in order to stay competitive, as a failure to forget can result in an inability to change.